

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
SUNSHINE DEVELOPERS, INC.,	:	DETERMINATION
JOSEPH MORRIS AND ROBERT MORRIS	:	
	:	
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Periods June 1, 1981	:	
through August 31, 1981 and June 1, 1984	:	
through August 31, 1984.	:	

Petitioners, Sunshine Developers, Inc., Joseph Morris and Robert Morris, 535 Secaucus Road, Secaucus, New Jersey 07094, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the periods June 1, 1981 through August 31, 1981 and June 1, 1984 through August 31, 1984 (File No. 802194).

A hearing was held before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, Two World Trade Center, New York, New York, on June 14, 1989 at 1:15 P.M., with all briefs to be submitted by October 16, 1989. Petitioners appeared at the hearing by Isidore Feldman, CPA. Petitioners' brief was submitted by Simon, Uncyk & Borenkind, Esqs. (Eli Uncyk, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (James Della Porta, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation properly assessed sales and/or use tax upon the purchase of two boats by Sunshine Developers, Inc. and the subsequent use within New York State of such boats.

II. Whether Joseph Morris and Robert Morris, officers of the corporation, may be held personally liable for payment of such sales and/or use taxes.

III. Whether petitioners have established reasonable cause for abatement of penalties assessed by the Division of Taxation.

IV. Whether petitioners are entitled to a credit for sales tax paid to the State of New Jersey on the purchase of the 50-foot Hatteras convertible.

FINDINGS OF FACT

In the early 1980's, the Division of Taxation undertook a boat audit program, i.e., it canvassed New York waters, surveyed marinas and obtained information from boat dealers for the primary purpose of identifying persons (and corporations) who purchased boats out of state and subsequently brought such boats into the State, thereby incurring potential sales or use tax

liability.

Based upon information obtained as a result of this audit program, the Division of Taxation, on April 24, 1985, issued to Sunshine Developers, Inc. (hereinafter "the corporation") and to Robert Morris and Joseph Morris a Notice of Determination and Demand for Payment of Sales and Use Taxes Due in the amount of \$76,390.00, plus penalty and interest, for a total amount due of \$103,953.00 for the quarters ending August 31, 1981 and August 31, 1984. The notice of determination contained the following explanation:

"Since you did not submit information requested in this Bureau's letters in connection with the purchase of a vessel, the following tax is determined to be due in accordance with the provisions of Section 1138 of the Tax Law.

Period <u>Ending</u>	*Tax <u>Due</u>	Penalty <u>Due</u>	Interest <u>Due</u>
08/31/81 - 182	\$24,165.00	\$6,041.00	\$11,599.00
08/31/84 - 185	52,225.00	6,267.00	3,656.00

*Represents tax due on:
1981 Hatteras - Sunshine - 50'
1984 Hatteras - Sunshine - 60"

The corporation was incorporated in Delaware on March 11, 1977. Since its incorporation, Robert Morris (980 shares) and his son, Drew Morris (20 shares), have been its only shareholders. At the hearing, Robert Morris could not recall what consideration was furnished to the corporation in exchange for its stock. Since its inception, Joseph Morris (president) and Robert Morris (secretary-treasurer) have been its only officers. The corporation's offices were located at 535 Secaucus Road, Secaucus, New Jersey. During the periods at issue, the corporation had no employees and maintained no offices other than its Secaucus address. The building wherein this office was located was also the primary business office of other corporations owned and/or operated by Robert and Joseph Morris (the sign on the front of this building did not set forth the names of each of these business entities, but, instead, read "The Morris Companies").

The corporation was formed for the stated purpose of purchasing, owning and operating boats. On or about April 8, 1977, the corporation purchased a 1977 33-foot Egg Harbor boat from Lake's Yacht Sales of Freeport, New York. On or about June 29, 1978, the corporation purchased a 1978 42-foot Post Fisherman boat from Anchorage Boat Sales, Inc. of Lindenhurst, New York. The purchases of these two boats were the subject of a prior assessment (Matter of Sunshine Developers, Inc. and Joe Morris, State Tax Commission, December 13, 1985, confirmed 132 AD2d 752, lv denied 70 NY2d 609) and are not, therefore, at issue herein.

The boats which are the subject of this proceeding are a 50-foot Hatteras Convertible purchased by the corporation in June 1981 from Lake's Yacht Sales, Inc. of Freeport, New York for \$345,210.00 and a 60-foot Hatteras Convertible purchased by the corporation in June 1984 from the same dealer for \$720,340.50. Both of these boats were named "Sunshine". No New York State sales tax was paid upon the purchase of any of the corporation's boats.

At the hearing held on the assessments issued as a result of the purchase and/or use of the boats in 1977 and 1978, petitioner Robert Morris testified that, from time to time, the corporation rented out its boats to other corporations owned by Robert and Joseph Morris. That hearing was held on September 11, 1984. It was, however, the testimony of petitioners at the hearing held herein that the boats at issue in this proceeding were never rented out. In support of their position, petitioners produced photocopies of the corporation's Federal income tax

returns which indicated that, for the years 1981 through 1983, the corporation was inactive. For 1984, the corporation reported a loss of \$156,286.00 primarily attributable to depreciation and interest payments. These returns indicated that the corporation received no income during any of these years. During the periods at issue, the corporation had no assets other than the boats and at no time did the corporation own more than one boat.

From 1977 until approximately 1984, petitioner Joseph Morris leased a rent-controlled apartment located at 1675 York Avenue, New York, New York. On the registration document for the 1981 50-foot Hatteras which was filed with the U.S. Coast Guard in November 1981, Joseph Morris listed the York Avenue apartment as his address.

From April 1, 1980 through February 28, 1985, petitioner Joseph Morris also leased an apartment at 555 North Avenue, Fort Lee, New Jersey. After the expiration of this lease, Joseph Morris moved to 604 Winston Towers, Cliffside Park, New Jersey, a condominium owned by petitioner Robert Morris since 1973. Joseph Morris continues to reside at this address.

Petitioner Robert Morris has continuously resided in the State of New Jersey from 1973 to the present.

The 1981 50-foot Hatteras Convertible was picked up by Joseph Morris at the Hatteras factory in New Bern, North Carolina on or about June 27, 1981. Joseph Morris took the boat to Ocean City, Maryland, Atlantic City, New Jersey and then to Montauk, New York where the boat was moored at the Deep Sea Yacht Club. During the summer of 1981, the boat was taken to Maine. At the conclusion of each boating season (approximately Labor Day), the boat was taken to Florida and the Bahamas.

The 1984 60-foot Hatteras was also picked up by Joseph Morris in New Bern, North Carolina. He took the boat to Ocean City, Maryland and then to the Deep Sea Yacht Club in Montauk, New York. During the 1984 boating season, the boat was taken to Block Island, Rhode Island, Nantucket, Martha's Vineyard and various other ports in Massachusetts and Maine. After Labor Day, the boat was navigated to Florida and the Bahamas.

From 1981 through 1984, a boat named "Sunshine" was moored at the Deep Sea Yacht Club in Montauk, New York during the summer boating season. Robert Darenberg, the dockmaster at the Deep Sea Yacht Club until June 1984, and Guy Lamotta, who became the dockmaster in June 1984, confirmed to the auditor that Joseph Morris had leased dock space for a boat named Sunshine during each of these seasons.

In April 1988, the New Jersey Department of the Treasury, Division of Taxation issued an assessment of sales and use tax to Joseph Morris in the amount of \$17,260.00, plus penalty and interest, for a total assessment of \$44,185.00 relative to the purchase of the 1981 Hatteras. On May 3, 1988, Joseph Morris paid the sum of \$19,470.00 in full satisfaction of this assessment.

Each of the boats at issue was purchased by the corporation and not by Joseph Morris and/or Robert Morris individually. There has been no evidence presented which would indicate that the corporation (a Delaware corporation with offices in New Jersey) maintained offices in New York or in any way carried on business or had any employees in New York.

The meeting of the board of directors (Joseph Morris was the sole member) which authorized the purchase by the corporation of the 1981 50-foot Hatteras was held at 634 City Island Avenue, City Island, New York. No explanation was provided for the location of this meeting.

At one time, the corporation had a bank account at the Flushing National Bank in New York. It is not clear from the record as to when this account was maintained. It should be noted that the corporation's 1983 Annual Franchise Tax Report filed with the State of Delaware was accompanied by a corporate check dated February 8, 1984 which was drawn on the National Community Bank of New Jersey.

Along with its brief, petitioners submitted six proposed findings of fact and four proposed conclusions of law. In accordance with the State Administrative Procedure Act § 307(1), petitioners' proposed findings of fact have been generally accepted and are contained within the Findings of Fact set forth hereinabove. The State Administrative Procedure Act does not require a ruling upon proposed conclusions of law.

The Division of Taxation also submitted, along with its brief, 30 proposed findings of fact which have been generally accepted with the following exceptions: proposed findings of fact "6" and "7" are accepted in part, but the reference to mooring at Deep Sea for at least two months a year is not supported by the evidence; proposed findings of fact "14" through "16", a portion of proposed finding of fact "17" and proposed findings of fact "18" through "21" and "29" each refer to witness recollection and, as such, are not deemed to be facts except as to the administrative law judge's ultimate determination of witness credibility (should such credibility be a determinative factor herein); proposed findings of fact "22" through "24" refer to a prior assessment not at issue herein and, except for certain references to such assessment and the resulting proceedings already set forth in the Findings of Fact hereinabove, are not deemed relevant to this proceeding; proposed findings of fact "27" and "28" are conclusory in nature; and proposed finding of fact "30" is not deemed relevant herein.

SUMMARY OF THE PARTIES' POSITIONS

The position of petitioners may be summarized as follows:

- (a) No sales tax was due on the purchase of the boats because delivery took place outside the State;
- (b) The purchases are also exempt from use tax because the corporation was a nonresident and did not carry on in the State any employment, trade, business or profession thereby exempting the corporation pursuant to the provisions of Tax Law § 1118; and
- (c) The Division of Taxation's basis for assessing petitioners Robert Morris and Joseph Morris is its contention that the creation of a Delaware corporation for the enumerated purposes was merely a tax avoidance scheme and, as such, the corporate veil should be pierced to hold petitioners personally liable. Petitioners contend that stock was issued, officers were appointed, tax returns were filed, etc., thereby establishing the viability of the corporation.

The Division of Taxation's position is as follows:

- (a) The boats at issue were subject to tax by virtue of the fact that since they were moored in New York during the summer months, such activity constituted a use within the meaning of Tax Law § 1101(b)(7);
- (b) The corporation's business (purchasing, owning and operating yachts) was conducted on a regular basis in New York and, as such, the corporation was a resident thereby subject to use tax. The Division points to the decision in Sunshine Developers,

Inc. v. Tax Commn. (supra) as authority for its contention that the corporation's activity of operating boats in New York constituted the conduct of business in the State. The Division also seeks to estop petitioners from contesting this residency issue on the basis of this court decision;

(c) In the alternative, the establishment of the corporation by Robert and Joseph Morris was a scam designed to avoid payment of sales and/or use tax and, as a result thereof, said petitioners should be held personally liable for tax assessed on the purchases and/or use of the boats; and

(d) Since petitioners failed to report or remit tax even after a decision by the State Tax Commission and by the Appellate Division of New York State Supreme Court (see, Finding of Fact "4") regarding similar issues, it cannot be held that they have a bona fide disagreement with the Division over application of the law. Penalty should, therefore, be sustained.

CONCLUSIONS OF LAW

A. 20 NYCRR 525.2(a)(3) provides, in pertinent part, as follows:

"The sales tax is a 'destination tax', that is, the point of delivery or point at which possession is transferred by the vendor to the purchaser or designee controls both the tax incident and the tax rate."

The evidence is uncontroverted that possession of both of the boats at issue was transferred in New Bern, North Carolina. Therefore, these transactions were not subject to the New York State sales tax imposed pursuant to Tax Law § 1105(a).

B. Tax Law § 1110 which imposes a compensating use tax provides, in pertinent part, as follows:

"Except to the extent that property or services have already been or will be subject to the sales tax under this article, there is hereby imposed on every person a use tax for the use within this state...except as otherwise exempted under this article, (A) of any tangible personal property purchased at retail...."

Tax Law § 1101(b)(former [7]) defines the term "use" as:

"[t]he exercise of any right or power over tangible personal property by the purchaser thereof and includes, but is not limited to, the receiving, storage or any keeping or retention for any length of time...."

The evidence obtained from the dockmasters at the Deep Sea Yacht Club in Montauk, New York indicates that a boat named "Sunshine" was moored there for at least a portion of every summer from 1981 through 1984 and that such space had been leased to petitioner Joseph Morris. While there is some dispute over the actual amount of time in which the boats were moored during these summer boating seasons, petitioners admit that the boats were, in fact, used in New York for some part of each summer.

C. Tax Law § 1118(2) provides that the following uses of property shall not be subject to the compensating use tax:

"In respect to the use of property purchased by the user while a nonresident

of this state, except in the case of tangible personal property which the user, in the performance of a contract, incorporates into real property located in the state. A person while engaged in any manner in carrying on in this state any employment, trade, business or profession, shall not be deemed a nonresident with respect to the use in this state of property in such employment, trade, business or profession."

Entitlement to the above use tax exemption must, therefore, turn on whether or not the corporation was a nonresident of New York and, even if determined to be a nonresident, whether or not the corporation was carrying on in the State any employment, trade, business or profession.

D. 20 NYCRR 526.15(b)(1) provides as follows:

"Any corporation incorporated under the laws of New York, and any corporation, association, partnership or other entity doing business in the State or maintaining a place of business in the State, or operating a hotel, place of amusement or social or athletic club in the State is a resident."

This corporation was incorporated under the laws of Delaware and did not maintain a place of business in the State. It must then be determined whether the corporation was doing business in the State. The New York State sales and use tax regulations contain no definition of the term "doing business" as this term applies to corporations. It is logical then to look to the business corporation franchise tax regulations for such a definition. 20 NYCRR 1-3.2(b) provides as follows:

"(1) The term doing business is used in a comprehensive sense and includes all activities which occupy the time or labor of men for profit. Regardless of the nature of its activities, every corporation organized for profit and carrying out any of the purposes of its organization is deemed to be doing business for the purposes of the tax. In determining whether a corporation is doing business, it is immaterial whether its activities actually result in a profit or a loss.

(2) Whether a corporation is doing business in New York State is determined by the facts in each case. Consideration is given to such factors as:

- (i) the nature, continuity, frequency, and regularity of the activities of the corporation in New York State, compared with the nature, continuity, frequency, and regularity of its activities elsewhere;
 - (ii) the purposes for which the corporation was organized, compared with its activities in New York State;
 - (iii) the location of its offices and other places of business;
 - (iv) the income of the corporation and the portion thereof derived from activities in New York State;
 - (v) the employment in New York State of agents, officers and employees;
- and
- (vi) the location of the actual seat of management or control of the corporation."

Petitioners contend that, during the years at issue, the corporation did not lease out its boats as it had done with respect to other boats in prior years. Its Federal income tax returns do not indicate that it received any income during these years. The Division of Taxation has produced no evidence that the corporation leased its boats or was engaged in any other income-producing activity either within or without the State. While most corporations are formed with income-producing activities in mind, it is not unusual to incorporate to insulate its principals from

personal liability.

The Division of Taxation argues that the corporate purpose was to purchase, operate and maintain vessels for recreational use. This is not disputed by petitioners. Furthermore, the Division argues that this is exactly what the corporation did in New York, i.e., purchase boats from a New York vendor (although it took delivery elsewhere) and operate and maintain such boats for recreational purposes. The above regulation defines "doing business" as "all activities which occupy the time or labor of men for profit" (emphasis added). Moreover, the factors to be given consideration as set forth in the regulation weigh heavily in favor of a determination that the corporation was not doing business in New York. The frequency and regularity of its activities in New York was, at most, two months per year. Its offices were located in New Jersey. It derived no income from its New York activities. It employed no agents, officers or employees in New York. While the corporation did, in fact, carry out activities in New York which were consistent with the purpose for which it was formed, this, alone, does not result in a determination that the corporation was doing business in New York.

The Division of Taxation points to the decision in Sunshine Developers, Inc. v. Tax Commn. (*supra*) as authority for the position that petitioners are estopped from contesting that the corporation is a New York resident. The Division's position is without merit in light of the difference in the facts between that case and the matter at issue herein. In the prior case, petitioners admittedly chartered their boats to other businesses. The Appellate Division found, therefore, that petitioners used the boats in New York (by seasonally mooring them in New York) plus that the corporation was not entitled to the exemption for nonresidents since it was engaged in carrying on a business in this State. It must be emphasized that this decision did not hold that the corporation was a resident, but, instead, held that, by virtue of the facts contained therein, it was not entitled to the exemption for nonresidents.

The facts in the present matter do not bar the corporation from entitlement to the nonresident exemption set forth in Tax Law § 1118(2). Petitioners' purchase of the boats at issue are, therefore, exempt from the imposition of use tax.

E. The Division of Taxation seeks to hold petitioners Joseph Morris and Robert Morris personally liable for sales or use taxes by virtue of its contention that the corporation was a sham which was formed for the primary purpose of evading New York sales and use taxes. In its proposed findings of fact, the Division wishes to draw an inference, from the inability of Joseph and Robert Morris to recall the names of insurance carriers, agents who filed incorporation papers in Delaware, the manner in which funds were acquired and expenses paid, etc., that the corporation was not a legitimate corporation and that the corporate veil should be pierced and the officers and shareholders be held personally liable for the taxes.

The United States District Court for the Eastern District of New York in Brunswick Corporation v. Waxman (459 F Supp 1222, *affd* 599 F2d 34) set forth an historical treatise on the corporate form of doing business. Citing Ballantine on Corporations (2-6 [1946]) and C. L. Israels, Corporate Practice (7-12 [1963]), the court stated that the corporate concept has three basic objectives, i.e., to provide limited liability, perpetual existence and transferability of shares. The court further stated that it is difficult, if not impossible, to formulate a precise set of circumstances under which a court should disregard the corporate form. However, the burden in each case rests upon the plaintiff to establish that there is a basis which serves for disregard of the corporate form (see, Coryell v. Phipps, 128 F2d 702, *affd* 317 US 406).

Citing Lowendahl v. Baltimore & O.R. Co. (247 App Div 144, 287 NYS 62, *affd* 272 NY 360), the Brunswick court set forth the following factors to be used to determine whether the corporate veil should be pierced:

"(1) domination and control over the corporation by those who are to be held liable which is so complete that the corporation has no separate mind, will, or existence of its own;

(2) the use of this domination and control to commit fraud or wrong or any other dishonest or unjust act; and

(3) injury or unjust loss resulting to the plaintiff from said control and wrong."

The law permits the incorporation of a business for the very purpose of escaping personal liability (Bartle v. Home Owners Co-Operative, Inc., 309 NY 103). This was clearly the purpose for which Sunshine Developers, Inc. was formed. While there can be no dispute that this corporation was dominated and controlled by petitioners Joseph and Robert Morris, this situation is certainly not unusual in any corporation owned and controlled by a very few persons.

While the Division of Taxation alleges that formation of the corporation in Delaware, taking delivery of the boats in North Carolina, etc. constitute fraudulent acts with intent to deprive the State of New York of its just sales and use tax revenues, the evidence produced herein does not support such allegation. This corporation had meetings of its board of directors, it issued shares of stock and it filed corporate tax returns. It may well be true that the capital used to purchase the boats came from Joseph and/or Robert Morris or from other corporations controlled by these petitioners and it may also be true that certain acts such as taking delivery of the boats were undertaken with the express intent of avoiding payment of sales or use taxes. However, a review of the evidence herein does not indicate fraud or wrongdoing, but merely that well-planned business practices designed to avoid taxation were effectuated.

Based upon the foregoing, it is hereby determined that the corporate veil must not be pierced herein and personal liability cannot, therefore, be imposed. Since the boats at issue were purchased and used by the corporation and such corporation has been absolved of liability for both sales (Conclusion of Law "A", supra) and use (Conclusion of Law "D", supra) taxes, the assessments for such taxes on all petitioners herein must be cancelled.

F. By virtue of Conclusion of Law "E", supra, Issues III and IV are rendered moot.

G. The petition of Sunshine Developers, Inc., Joseph Morris and Robert Morris is granted and the Notice of Determination and Demand for Payment of Sales and Use Taxes Due issued to said petitioners on April 24, 1985 is hereby cancelled.

DATED: Troy, New York
May 3, 1990

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE